Supreme Court of the United States

OCTOBER TERM, 1945

No.

MANHATTAN RAILWAY COMPANY and CHARLES FRANKLIN,
Petitioners,

against

THE CITY OF NEW YORK, *et al.*,
Respondents.

BRIEF IN SUPPORT OF PETITION

Statement of the Case

A summary statement of the facts is given in the petition (pp. 3-8 above).

Specification of Errors

It is submitted that the Court below erred:

1. In disregarding the question, raised by the summary dismissal of the first cause of action, whether the lien of petitioner Franklin attached to the fund recovered for the stockholders, regardless of the absence of any allegation that this recovery or the services performed in effecting it were of benefit to the receivership estate.

2. In overruling the contention that the general principle of equity upheld by this Court in *Sprague* v. *Ticonic Bank*, 307 U. S. 161 applied to the first cause of action.

3. In overruling the contention that the statutory lien provided for by state law sustained the first cause of action.

The question whether there could be any recovery under general principles of equity for professional services, not of benefit to the estate receivership estate which had been rendered to a group of stockholders in obtaining an award for them through the receivership proceedings, has not been answered in any of the numerous prior proceedings connected with this receivership, and still remains unanswered as a result of the opinion herein sought to be reviewed, and would seem not to have been answered by this Court.

The question whether there could be a lien on the share of certain stockholders in the entire group who consented to be represented by the committee retaining the attorney who rendered the services, was expressly left unanswered by the Circuit Court of Appeals for the Second Circuit in *Palmer* v. *Watson,* 122 F. (2d) 598, C. C. A. 2d.

As an outcome of the summary dismissal of the first cause of action herein upon the cross motion of the City of New York, the legal sufficiency of the allegations of the claim of petitioners to a lien upon the fund recovered for the benefit of stockholders, is involved. Both the Circuit Court and the District Court disposed of the first cause of action, in sustaining the cross motion of the City of New York for the dismissal thereof, without reference to the plea of *res judicata* based upon *Franklin et al.* v. *City of New York,* 144 F. 2d 571, C. C. A. 2d, certiorari denied, 324 U. S. 847, as set forth in the answer of the Committee for Manhattan's Guaranteed 7% Stock (R. 121, 127-135), or to the ground of *res judicata,* contained in the cross notice of motion of the City of New York (R. 239-241), except in so far as said ground for the cross motion was deemed to bar the present application upon the theory that all of its allegations were dependent upon

the existence of a contract right under the Plan of Unification.

The defense of *res judicata* will in no event be of avail to dispose of the first cause of action, because, as will hereinafter be shown, the statutory lien depends upon the adjudication made heretofore by the Circuit Court of Appeals for the Second Circuit that the fund was recovered on behalf of the stockholders of Manhattan upon the ground that they were creditors of Interborough.

ARGUMENT

POINT I

The opinion of the Circuit Court of Appeals disregards the equitable principle supporting the contention of petitioner Franklin that power resides in the District Court to enforce a lien on his behalf against the fund recovered through his efforts.

In *Sprague* v. *Ticonic Bank*, 307 U. S. 161, petitioner through suit in the Federal District Court brought on her own behalf and at her own expense, had vindicated her claim to a lien on the proceeds of earmarked bonds to the amount of her trust funds in the hands of the receiver of two insolvent banks. Petitioner alleged that by thus vindicating her claim she had established as matter of law the right of recovery in relation to numerous trusts in situations like her own. She, therefore, prayed the District Court for reasonable counsel fees and litigation expenses to be paid out of the proceeds of the bonds.

The petition was denied in the District Court as well as in the Circuit Court of Appeals upon the ground that the award of such costs was beyond the power of the District Court. This Court granted certiorari. In re-

versing, it held that the power did exist to make "such award, as between solicitor and client".

The growth of this jurisdiction of Chancery to make an award in favor of one litigant as against another originated from the analogous right of the solicitor to be allowed all his costs and expenses (in *Lomax* v. *Hide*, 2 Vern. 185 [1690]).

Chancery did not overlook the source of the principle after its continued application for more than a century. In *Dungey* v. *Angove*, 2 Ves. Jun. 304 (1794), the plaintiff tenant filed a bill of interpleader against his landlord, the defendant Angove, on notice of ejectment by a stranger under a title adverse to that of the landlord. From the nature of the suit, the Lord Chancellor suspected collusion and directed an inquiry. The ensuing report confirmed the fraud. Upon dismissal of the bill, "the plaintiff and his solicitor were ordered to pay all the expenses of the defendant Angove as between attorney and client * * *" 2 Ves. Jun. 304, at 313; 30 Eng. Rep. 644 at 649.

The uniform administration of equity exacts protection for an attorney or solicitor, in the absence of a retainer, through an award "as between solicitor and client" in instances where he had obtained a benefit for a party; when, under like circumstances, he might have been subjected to a proceeding for the purpose of recovering such an award against himself for causing loss to this same party.

Sprague v. *Ticonic Bank*, 307 U. S. *supra*, at 165, portrays the relevancy of eighteenth century English practice in contemporary equity suits. Although "a bankruptcy proceeding is not itself a suit in equity either by statutory definition or in common understanding" (*Columbia Gas Co.* v. *Amer. Fuel Co.*, 322 U. S. 379, 383), a court of bankruptcy "is guided by equitable doctrines and principles" (*Securities Comm.* v. *U. S. Realty Co.*, 310 U. S. 434, 455). A Federal District Court in matters arising out of an

equity receivership, instead of bankruptcy, does not have to modify or suspend these postulates to avoid inconsistency with the Chandler Act (*ibid*). Especially, does the role of the Chancellor provide the source of authority for the Federal Courts in exercising jurisdiction over these receiverships, as their jurisdiction owes its birth to the persistent vitality of equity, independently of statute, to supply new remedies (Finletter, The Law of Bankruptcy Reorganization, 5 ff; Dean, A. Review of the Law of Corporate Reorganizations, 26 Columbia Law Quarterly, 537). Since precedents in equity assumed binding effect in the period of Lord Eldon (Pound, The Decadence of Equity, 5 Columbia Law Review, 20, 25) its historic milestones must be heeded.

As the attempt to harmonize the subject of costs in the Federal courts was not made until 1853 (Street, Federal Equity Practice, § 1987) and the foundation of their power to prescribe costs in equity was not ultimately settled until the adoption in 1878 of §§ 917 and 918 of the Revised Statutes (Street, *supra,* § 1988) this legislation follows the era of the crystallization of equity (Pound, 5 Columbia Law Review, *supra,* at 25). Consequently, the operation of the rules and orders carrying out this legislation must apply equally from the standpoint of equity jurisprudence as well as from the norm of the due process clause of the Fifth Amendment to prevent discriminatory effect in a particular situation (see *Currin* v. *Wallace,* 306 U. S. 1, 14; cf. *Norwood* v. *Baker,* 172 U. S. 269, as explained in *French* v. *Barber Asphalt Paving Co.,* 181 U. S. 324, 344, 345).

In the instant case, petitioner Franklin might have advised the board of directors of the Manhattan Railway Company to proceed to eliminate the interests of its stockholders. His role as such adviser would probably have been particularly facile as the prospects of Unification and the approaching end of the receivership became in-

creasingly definite. At that period, *Case* v. *Los Angeles Lumber Co.,* 308 U. S. 106, had recently emphasized the necessity for subordination of stockholders to bondholders in corporate reorganization in accordance with the opinion in *Northern Pacific Ry. Co.* v. *Boyd,* 228 U. S. 482.

This aspect of the position of the Manhattan stockholders was definitively argued in 1941 before the Circuit Court of Appeals for the Second Circuit in *American Brake Shoe & F. Co.* v. *Interborough R. T. Co.,* 122 Fed. 2d 454, C. C. A. 2d, wherein Judge Patterson's order in the District Court upholding the Plan of Unification was affirmed.

In answer to the contention of Manheim, a holder of Manhattan Second Mortgage bonds, that the Manhattan shareholders should not participate, Judge Swan asserted in part (122 F. 2d at 459-460, C. C. A. 2d):

> "There remains to be considered the matter of the participation of Manhattan shareholders. In the Settlement Fund order they were alloted nearly $10,000,000, while the Second Mortgage bonds were allotted only about $1,800,000 and have not been paid in full. Manheim contends this is invalid under *Case* v. *Los Angeles Lumber Products Co.,* 308 U. S. 106, 60 S. Ct. 1, 84 L. Ed. 110. Had Manhattan assets been used to pay the shareholders instead of creditors the contention would be sound, but it must be remembered that Interborough's guaranty endorsed on the Manhattan stock certificates gave the stockholders a direct contract claim against Interborough. *Peabody* v. *Interborough R. T. Co.,* 212 App. Div. 502, 209 N. Y. S. 380; *Pennsylvania Steel Co.* v. *New York City R. Co.,* 2 Cir., 198 F. 721, 761. As such the compromise establishing their participation in the Settlement Fund was made between them and Interborough and not as participants in Manhattan assets. Consequently the Manhattan stockholders did not receive anything as stockholders, but rather as general creditors of Interborough—a position the same as the Manhattan Second Mortgage bondholders, who them-

selves were participating only as general creditors of Interborough—all Manhattan physical assets having been exhausted by the Manhattan Consolidated Mortgage prior lien."

The remaining paragraph devoted by Judge Swan to this discussion relates principally to the immunity of this compromise agreement from attack by the Second Mortgage Bondholders.

Hence, as the allegations of the first cause of action must be deemed true upon its summary dismissal herein, this opinion of Judge Swan furnishes adequate proof of the asserted success of petitioner in safeguarding the interests of the Manhattan stockholders as against their subordination to the bondholders.

Petitioner has been proven equally successful in his efforts to prevent the disaffirmance or modification of the terms of the lease of Manhattan to the Interborough. Thus, Judge Patterson in the course of his opinion approving the Plan of Unification said [*American Brake Shoe & F. Co.* v. *Interborough R. T. Co., Record on Appeal* (ff. 1198 at 1201, 1202)]:

> "In 1939 this court granted the application to disaffirm as to the lines leased from the Manhattan, but denied the application so far as it related to operation of the elevated extensions. In April 1939 the Circuit Court of Appeals reversed the decision. *Murray* v. *Roberts,* 103 F. 2d, 889 (C. C. A. 2). It was held that the Interborough could not get rid of an obligation to the City to operate the third tracks and extensions on the Manhattan property, and in effect that the receiver could not reject the Manhattan lease without consent of the City. The City's position on the issue had been that the Interborough receiver should not cease operation of the Manhattan system but that the terms of the lease were too onerous. From this decision there is now pending a petition for certiorari to the Supreme Court. Prosecution of the petition for certiorari and all other proceedings relative to the effect of fran-

chises on operating responsibilities and priorities of claimants have been held in abeyance for some months while a plan and agreement looking toward complete acquisition of the properties by the City has been in the course of negotiation and fulfillment."

Doubtless, as a part of this negotiation, after all of the properties subject thereto had been transferred to the City of New York, a stipulation was signed for the dismissal of the petitioners for certiorari in *Murray* v. *Roberts* (311 U. S. 720).

The contemporary relevancy of eighteenth-century English practice in respect of costs and allowances, as explained in *Sprague* v. *Ticonic Bank, supra,* makes unquestionable the power of the Federal District Court to pass upon the good faith of petitioner Franklin, in case he had induced the Manhattan Railway Company to take a position adverse to the claims of its stockholders, and they had been forced to retain counsel on their own behalf to obtain the funds in controversy. Proof of fraud or of bad faith would then have entitled them to an award "as between solicitor and client" against either Manhattan or Franklin or both (*Dungey* v. *Angove, supra*).

Sprague v. *Ticonic Bank, supra,* as we have seen, upholds the power of the Federal District Court to allow a single Manhattan stockholder who might have retained petitioner Franklin to perform the services actually rendered, to have charged upon the fund recovered the whole amount charged to him by Franklin, including the latter's fee as counsel.

With this equitable principle thoroughly established, petitioner Franklin has a right to enforce his claim for professional services upon the fund, which came into being through his professional labors under his retainer with the Manhattan Railway Company. Its board of directors and one of the two stockholders' protective committees are officially on record in support of his claim. The responsi-

ble heads of the other committee are individually on record to the same effect. As the authorities, which are herein relied upon, show, the award "as between solicitor and client" does not depend upon an express contract. To deprive petitioner Franklin of the hearing which he seeks in this proceeding to enable him to prove the value of his services, would be to deny a property interest to him through a discriminatory construction of federal equity jurisdiction and of the rule making power exercised by the Federal Courts pursuant to §§ 917 and 918 of the Revised Statutes. This result follows, since the basis of the doctrine invoked for an award "as between solicitor and client" is petitioner Franklin's right to a recovery of the value of the effort or expense caused by the litigation which was brought for the establishment of the fund. The Federal District Court, therefore, has and must exercise the power to enforce petitioner Franklin's equitable lien upon this fund. As this issue was not raised or brought to the attention of the courts in any way in *Franklin* v. *City of New York,* 144 F. 2, 57, C. C. A. 2d; certiorari denied, 324 U. S. 847, or by any prior proceeding, the present application is not barred (*Sprague* v. *Ticonic Bank,* 307 U. S., *supra,* 168 and note, explaining *Kansas City Southern Ry. Co.* v. *Guardian Trust Co.,* 281 U. S. 1).

The Circuit Court of Appeals took the position erroneously that petitioners herein were attempting in their first cause of action to enforce their equitable liens upon the premise of the assumption by the City of New York, under the Plan of Unification of the contractual obligation created by the retainer of petitioner Franklin by petitioner Manhattan. The erroneous nature of this position is illustrated by the affirmance of the order of dismissal entered in the District Court upon the cross motion of the City of New York. The first cause of action is not brought to obtain further allowances from the City of New York. Its sole object is to impress a lien upon funds established for the benefit of stockholders by petitioner Franklin.

POINT II

The fund in controversy was recovered on behalf of the stockholders of the Manhattan Railway Company, who have been adjudged general creditors under the Plan of Unification.

As the Protective Committee for the holders of the Modified Guaranteed 5% Stock of the Manhattan Railway Company retained petitioner Franklin and agreed to compensate him for his services in effecting this recovery, he has the right to apply directly, without any intervention by said stockholders or their representatives, for payment out of the fund. Under the law of the State of New York, his right to enforce a statutory lien arises from the absence of an express contract authorizing recovery of payment thereunder.

The stockholders of Manhattan had a direct contract claim against Interborough (*American Brake Shoe & F. Co.* v. *Interborough R. T. Co.*, 122 Fed. 454 at 460, C. C. A. 2d; see quotation thereof under Point I, herein, *supra* (pp. 15-16). In concluding the second paragraph of that discussion, previously referred to herein without quotation (*ibid*), Swan, J., declared (122 F. (2d) *supra* at 460):

> "As the settlement was made by Interborough to dispose of the stockholder claims it is very doubtful whether any infirmity in the stockholders' legal position could benefit the Manhattan Second Mortgage bondholders. More important, however, is the fact that the settlement order, the validity of which we have already sustained, established by compromise the legal rights of the Manhattan stockholders to share as creditors, so that now their status as such cannot be questioned. As participation of Manhattan stockholders was in the capacity of general creditors of Interborough, a status not inferior to the Manhattan Second Mortgage bonds, it cannot be attacked by Manheim as a holder of such bonds."

The principle elucidated in *Ticonic Bank* v. *Sprague, supra,* to allow recovery of an award "as between solicitor and client" to one who sued for the benefit of a trust estate, was recognized in *Trustees* v. *Greenough,* 105 U. S. 527. It was stated therein (*supra,* 533), as quoted by this Court in *Central Railroad* v. *Pettus,* 113 U. S. 116, 123, that "the same rule is applicable to a creditor's suit where a fund has been realized by the diligence of the plaintiff."

In *Central Railroad* v. *Pettus,* the Court stated further (p. 123):

> "We have seen that the purchase, by the Western Railroad Company of the property of the Montgomery and West Point Railroad Company, and the surrender by the latter of its charter, left the unsecured creditors of the vendor company unprovided for, except as the vendee company assumed and agreed to meet the outstanding debts and obligations of the other company. But when the present appellants became purchasers at the sale in the suit instituted by Morris and Lowery, trustees, they asserted their right to hold the property, originally belonging to the Montgomery and West Point Railroad Company, freed from any claim against it by the unsecured creditors of that company. Those creditors resided in several States, and their claims aggregated a large amount. Co-operation among them was impracticable. If some did not move, the interests of all would have suffered. Hence Branch, Sons & Co. and their co-complainants instituted suit for the benefit of themselves and other creditors of the same class. They, and their solicitors, bore the entire burden of the litigation until the lien was finally declared, and the property ordered to be sold to pay all claims filed pursuant to the decree."

These circumstances furnish a close parallel to those existing in August 1939 in relation to the precarious position of the Manhattan stockholders. The claim of the right of Interborough to disaffirm the 1913 lease, and the contention of the Manhattan bondholders to priority over

the stockholders, still awaited definitive adjudication. Judicial notice may be taken of the wide distribution of a large volume of Manhattan stock throughout the United States. Although the City of New York in acquiring the properties under the Plan of Unification did not dispute the stockholders' rights, such rights, as we have explained, would have been previously extinguished without petitioner's positive aid, as alleged herein under the first cause of action.

Under these circumstances, the following paragraph of the opinion in *Central Railroad* v. *Pettus, supra,* is peculiarly apposite (113 U. S. at 124-125):

> "It is clear that within the principles announced in *Trustees* v. *Greenough,* Branch, Sons & Co. and their co-complainants are entitled to be allowed, out of the property thus brought under the control of the court, for all expenses properly incurred in the preparation and conduct of the suit, including such reasonable attorney's fees as were fairly earned in effecting the result indicated by the final decree. And when an allowance to the complainant is proper on account of solicitors' fees, it may be made directly to the solicitors themselves, without any application by their immediate client."

It is thus plain that the Circuit Court of Appeals misapprehended the purpose of the instant application in purporting to dispose of it upon the ground announced in the prior application "that allowance of counsel fees is controlled by the benefit brought to the receivership estate."

In the instant proceeding, the first cause of action is based upon sections 474 and 475 of the Judiciary Law of the State of New York. In the closely related field of bankruptcy, it was held by Judge Patterson in the Southern District of New York, in a proceeding emanating from the reorganization in the case of *In re McCrory Stores Corporation* (1937), 19 F. Supp. 691, 694:

> "In bankruptcy the attorney for a creditor does not acquire a lien on the filing of the bankruptcy petition, and he certainly does not at any time have a lien on the general assets of the estate. So far as he and his lien are concerned, the 'commencement' of the action or proceeding referred to in the New York statute providing for an attorney's lien is the filing of the proof of claim, and the lien is only on the claim and later on the fund allocated to payment of the claim. In fact, the action or proceeding in the sense of the statute is not the bankruptcy proceeding as a whole, but is the proceeding initiated by the filing of the proof of claim."

Through this interpretation of the New York statute, the force of *Central Railroad* v. *Pettus, supra,* gains strength from the additional circumstances occurring therein that after the decree in the original litigation, commenced and prosecuted wholly in the state courts of Alabama, the defendant corporations bought up the claims of unsecured creditors, including those of the complainants. As to that factual situation, this Court declared (113 U. S., *supra,* 127-128):

> "The lien of the solicitor rests, by the law of that state, upon the basis that he is to be regarded as an assignee of the judgment or decree, to the extent of his fees, from the date of its rendition. This right of the solicitors is superior to any which the defendant corporations acquired, subsequent to the decree, by the purchase of the claims of unsecured creditors."

The first cause of action in the instant proceeding, therefore, seeks to enforce a lien, both equitable and statutory. Under the statute this lien had its inception at the commencement of the proceeding to enforce the claim (*In re McCrory Stores Corporation,* 19 F. Supp. 691) and subsequently attached to the fund recovered as a result of the aforesaid proceeding (*ibid*). This lien upon the fund allo-

cated to the claim is superior to the right of the holder of the claim (*ibid*) or to a purchaser from him (*Central Railroad* v. *Pettus*, 113 U. S., *supra*, at 127-128) and may be made directly to the attorney without any application by the client (113 U. S., *supra*, at 124-125).

In cases decided by the state courts of New York where the existence of the right to a common law possessory lien was at issue, it has been held that its non-existence was a condition precedent to an action by its putative possessor for recovery of a personal judgment (*Shoyer* v. *Wright-Ginsberg Co.*, 240 N. Y. 223, 233; *Newburger-Morris Co.* v. *Talcott*, 219 N. Y. 505, 511). By parity of reasoning, the New York Court of Appeals might hold that the right of an attorney to recover under an implied contract, as is provided for by section 474 of the Judiciary Law, and to enforce the correlative right to a lien under section 475 of this Law, would necessarily be available to petitioner Franklin when the effort to establish an express contract right against the City of New York has proved fruitless in the federal courts. As the opinion herein sought to be reviewed has avowedly made the allowances hitherto granted to petitioner, Franklin, solely upon the ground of benefit to the estate, the instant petition rests upon the theory of recovery for the independent benefits received by the stockholders. For this reason, petitioner Franklin has set forth facts sufficient to recover under the doctrine of money had and received to prevent unjust enrichment in accordance with New York law (*Schank* v. *Schuchman*, 212 N. Y. 352, 358; cf. *Thompson* v. *Magnolia Petroleum Company*, 309 U. S. 478). Federal authority permits analogous relief in a bankruptcy reorganization without the necessity for resort to the state tribunals (*In re McCrory Stores Corporation*, 19 Fed. Supp. 691).

CONCLUSION

The petition for a writ of certiorari should be granted.

Dated, New York, February 4, 1946.

Respectfully submitted,

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